CREDO
WEALTH

Chubb: Unexpected Titan

Established in the 8th Century BC, the Oracle of Delphi was famed for a prescience market forecasters can only aspire to. The trick, however, was that her pronoucements were shrouded in ambiguity. The tyrants of the time followed her advice, but their hubris proved their downfall: the Oracle's advice proved true, yet not in a manner they expected. In later years, the Oracle pronounced Socrates the wisest of all men, for he knew his own ignorance. It goes without saying that, at Credo, we favour the latter approach. A few months back we added Chubb to our portfolios based on a shrewd analysis of the fundamentals in an out of favour industry. In a Delphic turn of events, our analysis was rewarded, though not in the manner we anticipated.

With market and macroeconomic risks abounding, our thesis was grounded in Chubb's record discount to the market, low correlation, and stable earnings stream. However, it seems that we were not the only ones to find value in an industry forsaken by many. In early July, ACE announced it would acquire Chubb in a $28bn deal, valuing their fellow insurer at a 30% premium to its market value. Comprised of approximately 50% cash and 50% ACE stock, the deal was warmly welcomed by investors. Following the announcement, the stock price of both target and acquirer rose, implying that the whole was deemed greater than the sum of its parts. This is to say, the deal was expected to create value.

However, herein lies the oracular element: while our analysis uncovered the compelling value proposition that Chubb offered, we by no means anticipated that our efforts would be so soon rewarded. Of what remained of our original thesis, any further upside remains to be seen. While the deal offers an enticing (though approximate) $10 billion of value through synergies, the full extent of these are largely reflected in the stock price. Less clear is the potential for revenue synergies – where the company's combined product suite finds new clients within their combined client base. As this new titan gestates, it is evident that our upside expectations have already been fulfilled; what remains is uncertainty.

Moreover, deals of such scale carry significant execution risks. For instance, the unsuccessful courting of Syngenta by rivals Monsanto. While Syngenta's board were unwilling to even enter talks with Monsanto, and Chubb's management and shareholders have so far proved receptive to the deal, the risk remains and should not be overlooked.

Unlike the Oracle, we are furnished with no foresight. Nevertheless, by dint of fortune, our analysis has so far proved correct. Yet humility is more becoming than hubris – unlike the tyrants of the ancient world, we do not intend to overreach. Our analysis has been favoured, albeit unexpectedly, but now the outlook has changed. Revenue synergies are uncertain, break risks exist, and with approximately 50% of the deal being offered in ACE shares, we have decided to realise the profits of our labours and return to the search for worthy investments.

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